

**VIRGINIA COMMUNITY COLLEGE SYSTEM
RICHMOND, VIRGINIA**

**REPORT ON AUDIT
FOR THE YEAR ENDED
JUNE 30, 2002**



AUDIT SUMMARY

Our audit of the Virginia Community College System for the year ended June 30, 2002, found:

- The financial statements are presented fairly, in all material respects;
- internal control matters that we consider reportable conditions; however, we do not consider any of these to be material weaknesses;

These matters are reported fully in the section of the report entitled “Internal Control and Compliance Findings and Recommendations” and include our recommendation that the Virginia Community College System ensure the Colleges and the System have current information security plans.

- instances of noncompliance required to be reported that are described fully in the section of the report entitled “Internal Control and Compliance Findings and Recommendations”; and
- adequate corrective action of prior audit findings.

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April 30, 2003

The Honorable Mark R. Warner
Governor of Virginia

The Honorable Kevin G. Miller
Chairman, Joint Legislative Audit
and Review Commission

The State Board for Community Colleges

We have audited the accounts and records of **Virginia Community College System**, as of and for the year ended June 30, 2002, and submit herewith our complete reports on financial statements and compliance and internal control over financial reporting.

INDEPENDENT AUDITOR'S REPORT ON FINANCIAL STATEMENTS

We have audited the accompanying basic financial statements of Virginia Community College System, a component unit of the Commonwealth of Virginia, as of June 30, 2002 and for the year then ended, as listed in the table of contents. These financial statements are the responsibility of the System's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in Government Auditing Standards, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the System as of June 30, 2002, and the changes in its financial position and its cash flows for the year then ended, in conformity with accounting principles generally accepted in the United States of America.

As described in Note 1, the System has implemented a new financial reporting model, as required by the provisions of GASB Statement 34, *Basic Financial Statements - and Management's Discussion and Analysis - for State and Local Governments* and GASB Statement 35, *Basic Financial Statements - and Management's Discussion and Analysis - for Public Colleges and Universities*, as of June 30, 2002.

The Management's Discussion and Analysis on pages seven through twelve is not a required part of the basic financial statements but is supplementary information required by the Governmental Accounting Standards Board. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the required supplementary information. However, we did not audit the information and express no opinion on it.

INDEPENDENT AUDITOR'S REPORT ON COMPLIANCE AND ON INTERNAL CONTROL OVER FINANCIAL REPORTING

In planning and performing our audit of the financial statements of the Virginia Community College System as of and for the year ended June 30, 2002, we considered internal controls over financial reporting and tested compliance with certain provisions of laws, regulations, contracts, and grants in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in Government Auditing Standards.

Compliance

As part of obtaining reasonable assurance about whether the Virginia Community College System's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts and grants, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed instances of noncompliance that are required to be reported under Government Auditing Standards. These instances of noncompliance are described in the section of the report titled "Internal Control and Compliance Findings and Recommendations."

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the System's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control over financial reporting. However, we noted certain matters involving the internal control over financial reporting and its operation that we consider to be reportable conditions. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over financial reporting that, in our judgment, could adversely affect the System's ability to record, process, summarize, and report financial data consistent with the assertions of management in the financial statements. Reportable conditions, entitled "Update Information Security Plan" and "Enhance Fixed Asset Procedures" are described in the section of the report titled "Internal Control and Compliance Findings and Recommendations."

A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. However, we believe that none of the reportable conditions described above is a material weakness.

Status of Prior Findings

The System and its Colleges have taken adequate corrective action with respect to audit findings reported in the prior year report.

The "Independent Auditor's Report on Compliance and on Internal Control Over Financial Reporting" is intended solely for the information and use of the Governor and General Assembly of Virginia, the State Board for Community Colleges, its audit committee and management, and is not intended to be and should not be used by anyone other than these specified parties. However, this report is a matter of public record and its distribution is not limited.

EXIT CONFERENCE

We discussed this report with management at an exit conference held on June 27, 2003.

AUDITOR OF PUBLIC ACCOUNTS

KSA:whb
whb:66

INTERNAL CONTROL AND COMPLIANCE FINDINGS AND RECOMMENDATIONS

Update Information Security Plan

Applicable to: Virginia Community College System

Since 1998, the System Office has not updated the Office's comprehensive information security plan to reflect its current operating environment. The System Office has not updated the business impact analysis or risk assessment to form the basis for an updated comprehensive information security plan. Since last updating the comprehensive information security plan, the System has implemented a new administrative system.

Not updating the information security plan, business impact analysis, or risk assessment timely increases the costs of updating and if the plan becomes too stale, management may find that it would need to replace the entire plan from scratch. A plan that is nearly 5 years old will require a substantial revision.

These documents represent the System Office's and the individual college's responses to some of the basic computer safeguards that every entity needs to take to protect its assets. The System has to protect not only its physical assets, but also the data that it stores. This lack of timely update of security and risk evaluations at individual colleges has been the subject of two internal audit reports.

System Office information technology management issued general guidance to the colleges in 1998 to help them develop comprehensive security plans. The colleges were expected to develop plans using those guidelines; however, System management never followed-up with the colleges and has not provided additional guidance to the colleges on reviewing or updating their comprehensive security plans.

System Office information technology management is updating the guidance it issued in 1998, and it should issue that guidance as soon as possible. System management must provide guidance, training, deadlines, and follow-up to ensure that the System and the colleges have current comprehensive security plans to protect the System's information and resources.

Enhance Fixed Asset Procedures

Applicable to: Blue Ridge Community College
Germanna Community College
J. Sargeant Reynolds Community College
Patrick Henry Community College
Paul D. Camp Community College
Rappahannock Community College
Southside Virginia Community College
Virginia Highlands Community College
Virginia Western Community College

The fixed asset coordinators at these colleges do not always properly record all fixed asset changes in the Fixed Asset Inventory System and do not follow adequate fixed asset accounting and control procedures.

- Blue Ridge, Germanna, Rappahannock and Southside Virginia failed to remove disposed assets from the Fixed Asset Inventory System.
- J. Sargeant Reynolds did not complete an equipment inventory within two years as required by Section 30500 of the Commonwealth Accounting Policies and Procedures Manual.
- Patrick Henry failed to dispose of one item listed as surplus on the Fixed Asset Inventory System. The College also does not document the disposition of disposed items.
- Paul D. Camp failed to properly record two purchases in the Fixed Asset Inventory System.
- Virginia Highlands does not maintain proper separation of duties over fixed assets. The accountant who records and adjusts the Fixed Asset Inventory System, performs the College's physical inventory, and reconciles the fixed asset records to the Financial Records System. Additionally, there is no supervisory review of fixed asset transactions including adjustments and reconciliations. Also, the College lacks formal written procedures for conducting a physical inventory.
- Virginia Western failed to record the correct nomenclature code, which assigns useful life for depreciation, on three of six tested fixed asset purchases. Also, we found two of thirteen tagged assets not recorded in the Fixed Asset Inventory System. Additionally, eight of ten scales in the Dental Lab did not have inventory identification tags.

Each College's Fixed Asset Coordinator should review and document fixed asset procedures for the proper recording of asset records. College management should ensure that the Coordinators receive adequate training to record all fixed asset purchases and changes accurately and promptly. The System's Office should ensure the Coordinators receive training on the importance of nomenclature codes in the calculation of depreciation. Finally, management should commit the necessary resources to complete required equipment inventories and promptly resolve and record all discrepancies.

Properly Administer Return of Title IV Funds

Applicable to: Dabney S. Lancaster Community College,
New River Community College,
Southside Virginia Community College,

Dabney S. Lancaster Community College and Southside Virginia Community College did not always record and post Title IV refunds in a timely manner. Both colleges performed Title IV refund calculations timely and accurately; however, the two colleges failed to promptly return federal funds to the federal Department of Education. Additionally, New River Community College did not properly calculate Title IV refunds since they incorrectly calculated the number of days in their scheduled breaks.

34 CFR Part 668.22 (c) requires that colleges have a mechanism in place to identify students who have withdrawn or ceased attendance, in order to promptly and properly calculate any return of Title IV funds. Part 668.22 (j) requires that colleges return unearned Title IV funds as soon as possible to the federal Department of Education, but no later than 30 days after the date the college determined the student withdrew. 34 CFR Part 668.22 (f) requires the exclusion of scheduled breaks of five or more days, including weekends, in the calculation of Title IV refunds.

Colleges should follow the return of Title IV funds procedures prescribed by the federal government to ensure that withdrawals are properly identified and that refunds are properly calculated and returned to the U.S. Department of Education.

Provide Campus Security Report to All Current and Perspective Students and Employees

Applicable to: Dabney S. Lancaster Community College
Southside Virginia Community College
Southwest Virginia Community College

Dabney S. Lancaster Community College did not completely prepare and directly provide to students and employees their annual campus security report. Southside Virginia Community College and Southwest Virginia Community College did not directly provide to students and employees their annual security report.

34 CFR 668.41(e) requires that currently enrolled students and employees receive the institution's annual campus security report in its entirety through publications, mailings, or electronic media sent directly to individuals. According to the above requirement, colleges can post this report to a web site, but they must make available to each student a notice that identifies the information required to be disclosed; provides the exact electronic web site address; states that upon request, the individual is entitled to a paper copy; and informs the individual how to request a paper copy.

Colleges should comply with standards set forth by the Department of Education requiring preparation and direct notification of the annual security report.

MANAGEMENT DISCUSSION AND ANALYSIS

The following discussion and analysis provides an overview of the financial position and activities of the Virginia Community College System (VCCS) for the year ended June 30, 2002. This discussion has been prepared by management and should be read in conjunction with the financial statements and footnotes. In this first period of reporting under GASB 35, the VCCS has elected to not restate prior periods for the purpose of providing comparative data. However, in future years, when prior year information is available, a comparative analysis of financial data will be presented.

Financial Highlights

The following events impacted net assets of the VCCS in fiscal year 2002:

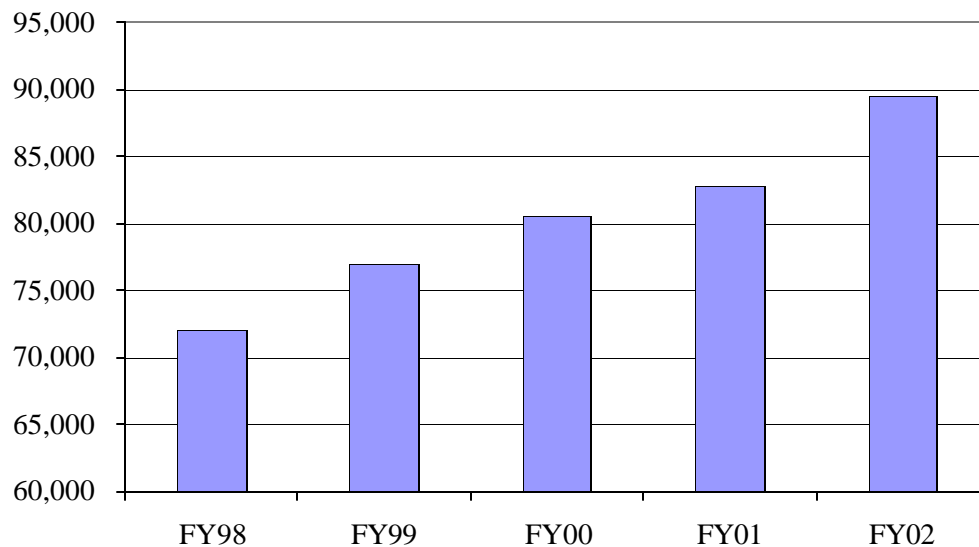
- During fiscal year 2002, the Commonwealth of Virginia realized a general fund budget shortfall. This shortfall was largely attributed to the national economy and significantly impacted the stock market and the revenues of the Commonwealth. This shortfall resulted in the VCCS reverting 3 percent of its general fund appropriations (less debt service and amounts earmarked for lease payments) or \$9.2 million.
- \$14.6 million of VCCS carry-forward funds reverted to the Commonwealth at the end of fiscal year 2001. These dollars are general and non-general funds largely committed to encumbrances and represent approximately 3 percent of the VCCS Educational and General fund budget. The VCCS typically is re-appropriated these funds in the subsequent fiscal year. However, \$2.6 million of the \$14.6 million was not returned to the VCCS in fiscal year 2002.
- Near the end of fiscal year 2002, the Commonwealth allowed state agencies, including colleges and universities, to prepay anticipated budget cuts for fiscal year 2003. This strategy was designed to help the Commonwealth resolve a cash shortage at year-end. The VCCS submitted \$5.6 million towards this prepayment that resulted in a significantly lower reversion at the end of fiscal year 2002.

Net assets increased by \$18.3 million principally due to the purchase and construction of fixed assets and increased prepaid expenses. Debt increased by a net amount of \$3.5 million. Additional debt of \$7.3 million was incurred to finance construction of the parking deck at the Northern Virginia Community College Medical Education Campus. \$6 million of the bond proceeds were unspent as of June 30, 2002. Capital lease obligations were reduced \$3.5 million.

Enrollment Information

Enrollments are at an all-time high at the VCCS. Below is a chart depicting full-time equivalent students attending the VCCS over the past 5 years. The VCCS mission is to provide comprehensive higher education and workforce training programs and services of superior quality that are financially and geographically accessible and that meet individual, business, and community needs of the Commonwealth.

VCCS Enrollment - Full Time Equivalents



One full time equivalent represents 30 credit hours of classes taken by a student over an academic year. It is calculated on an annual basis by taking the total credit hours taught divided by 30.

Financial Statements

The three financial statements presented are the Statement of Net Assets; the Statement of Revenues, Expenses, and Change in Net Assets; and the Statement of Cash Flows.

Statement of Net Assets

The Statement of Net Assets presents the assets and liabilities of the VCCS at the end of the fiscal year. The Statement also provides the amount of net assets and their availability for expenditure. Net assets are divided into three major categories. The first category, invested in capital net of related debt, consists of capital assets, net of accumulated depreciation and reduced by outstanding balances of any borrowings that are attributable to the acquisition, construction, or improvement of those assets. The next category is restricted net assets, which are classified as nonexpendable or expendable. Nonexpendable restricted net assets are permanent endowments that are available for investment purposes only and loan funds. Expendable restricted net assets are available for expenditure by the VCCS but must be spent for purposes determined by external entities. Unrestricted net assets are not subject to externally imposed restrictions and may be designated for specific purposes by management of the VCCS.

A summarized Statement of Net Assets as of June 30, 2002 is as follows:

| (In thousands of dollars) | |
|---|-------------------|
| Assets: | |
| Current assets | \$ 90,126 |
| Capital assets, net | 422,790 |
| Other assets | <u>32,713</u> |
| Total Assets | <u>545,629</u> |
| Liabilities | |
| Current liabilities | 63,137 |
| Non-current liabilities | <u>54,422</u> |
| Total Liabilities | <u>117,559</u> |
| Net Assets | |
| Invested in capital assets, net of debt | 385,963 |
| Restricted-nonexpendable | 452 |
| Restricted-expendable | 23,797 |
| Unrestricted | <u>17,859</u> |
| Total Net Assets | <u>\$ 428,071</u> |

Current assets consist primarily of cash and investments of \$75.4 million (including appropriations available of \$5.8 million), accounts and notes receivable of \$8.3 million, and prepaid expenses of \$4.7 million at June 30, 2002.

Capital additions were equipment and library book purchases of \$14.4 and \$1.9 million, respectively. Construction-in-progress additions during the year were principally comprised of \$19.3 million at Northern Virginia Community College for the Medical Education Campus, \$2.4 million at Tidewater Community College for the Advanced Technology Center, \$1.8 million at Thomas Nelson Community College for the Instructional Support Building, \$1.4 million at Blue Ridge Community College for the Business Technology Center, and \$1.3 million for the Working Development Center at Paul D. Camp Community College. These projects were funded with state appropriations, local appropriations, and bond proceeds of \$10.0, \$10.4 and \$5.5 million, respectively.

Other assets are principally cash, investments, and appropriations available for the purchase of fixed assets.

At June 30, 2002, the VCCS had future commitments for construction contracts totaling \$31.0 million. Commitments are primarily comprised of \$19.3 million for Medical Education Campus at Northern Virginia Community College, \$2.4 million for the Advanced Technology Center at Tidewater Community College and \$1.4 million for the Business Technology Center at Blue Ridge Community College.

Current liabilities consist primarily of accounts payable of \$13.4 million, accrued compensation of \$29.4, deferred revenue of \$11.2 million, and debt obligations of \$5.9 million. Noncurrent liabilities are comprised of accrued leave of \$12.3 million, long-term debt of \$37.6 million, and amounts due to the federal government of \$4.5 million.

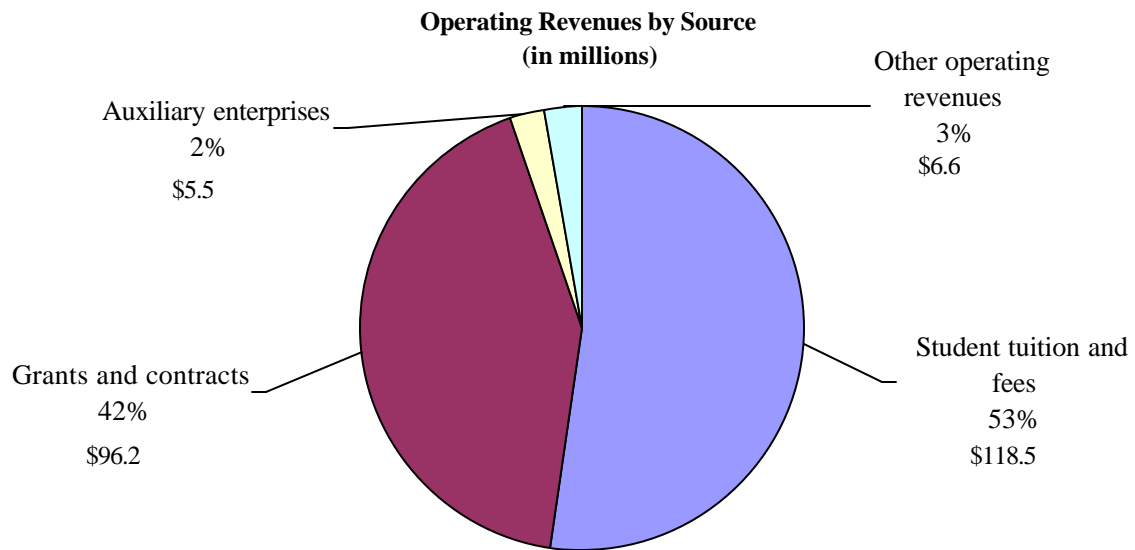
Statement of Revenues, Expenses, and Changes in Net Assets

The purpose of the Statement of Revenues, Expenses, and Changes in Net Assets is to present operating and non-operating revenues received by the institution, operating and non-operating expenses incurred, and any other revenues, expenses, gains, and losses. Changes in net assets as presented on the Statement of Net Assets are based on the activity presented in the Statement of Revenues, Expenses, and Changes in Net Assets.

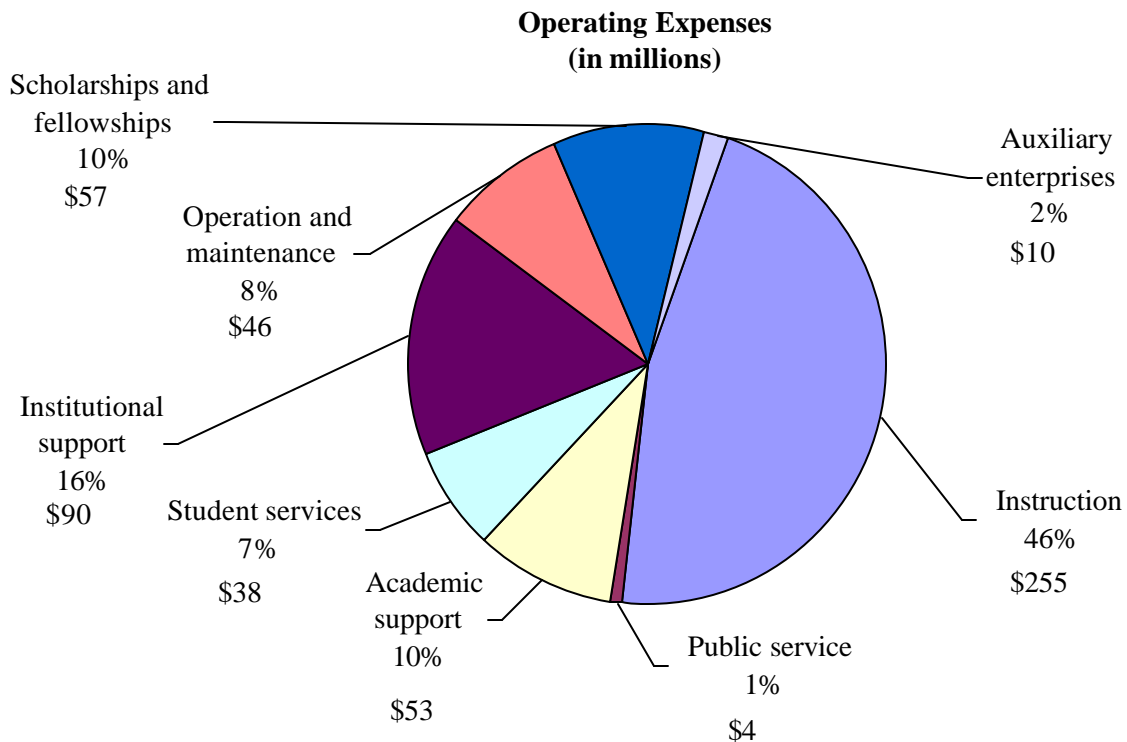
A summarized statement of revenues, expenses and changes in net assets for the year ended June 30, 2002 is as follows:

| | (In thousands of dollars) | |
|--|---------------------------|--------------------------|
| Operating revenue | | \$ 245,597 |
| Operating expenses | | <u>554,075</u> |
| Operating loss | | <u>(308,478)</u> |
| Nonoperating revenues (expenses): | | |
| State appropriations | | 307,015 |
| Private gifts, grants and local appropriations | | 2,633 |
| Investment income | | 1,575 |
| Interest expense | | (2,183) |
| Other | | <u>(1,598)</u> |
| Net nonoperating revenues | | <u>307,442</u> |
| Income (loss) before other revenues, expenses, gains or losses | | <u>(1,036)</u> |
| Capital appropriations | | 11,842 |
| Capital gifts/grants | | <u>7,512</u> |
| Increase in net assets | | <u>18,318</u> |
| Net assets, beginning of year as restated | | <u>409,753</u> |
| Net assets, end of year | | <u><u>\$ 428,071</u></u> |

A graphic presentation of operating revenues by source is below:



A graphic presentation of operating expenses by major function is below:



Statement of Cash Flows

The Statement of Cash Flows provides additional information about the financial results of the VCCS by reporting the major sources and uses of cash. A summary of the cash flows is as follows:

| (In thousands of dollars) | |
|---|-------------------|
| Net cash used in operations | \$ (295,838) |
| Net cash provided by non capital financing activities | 310,146 |
| Net cash used in capital and related financing activities | (27,183) |
| Net cash used by investing activities | <u>(77)</u> |
| Net increase (decrease) in cash and cash equivalents | (12,952) |
| Cash and cash equivalents, beginning of year | <u>114,435</u> |
| Cash and cash equivalents, end of year | <u>\$ 101,483</u> |

Economic Outlook

The VCCS is highly dependent on the Commonwealth for financial support. In fiscal year 2002, more than 70 percent of the VCCS educational and general funds were received from the Commonwealth's general fund. Due to the recent downturn in the national and Virginia economy, Commonwealth's revenue collections have not been sufficient to support the anticipated expenditures of state agencies. This resulted in 3 percent general fund budget cuts to the VCCS in fiscal year 2002. In addition, the Virginia General Assembly has assessed additional budget cuts for state agencies in the 2002-2004 biennium. The budget cuts for the VCCS are \$13.2 million (4.3 percent of VCCS general fund budget) in fiscal year 2003 and \$18.1 million (5.9 percent of the VCCS general fund budget) in fiscal year 2004. These cuts are reflected in the general fund appropriation in the *2002 Virginia Acts of the Assembly* (Chapter 899). The VCCS also lost \$4.4 million in Equipment Trust funding from the previous fiscal year due to the Commonwealth's budget shortfall.

To partially offset the 3 percent general fund cuts assessed to the VCCS in the 2002-2004 biennium, the State Board for Community Colleges increased tuition by 9 percent for in-state and out-of-state students beginning in the Summer Term 2002. In addition, to help offset the anticipated loss of \$4.4 million in Equipment Trust Funding in the 2002-2004 biennium, the State Board for Community Colleges increased technology fees by \$1.50 per credit hour to \$3.00 per credit hour beginning in the Summer Term 2002.

In October, additional budget cuts of \$23.8 million (8 percent of the VCCS general fund budget) and \$28.9 million (10 percent of the VCCS general fund budget) were accessed for fiscal years 2003 and 2004, respectively. To help offset this loss of funding, the State Board for Community Colleges increased tuition \$12.25 per credit hour for in-state and out-of-state students beginning in the Spring Term 2003.

FINANCIAL STATEMENTS

VIRGINIA COMMUNITY COLLEGE SYSTEM
STATEMENT OF NET ASSETS
As of June 30, 2002

| ASSETS | |
|---|-----------------------|
| Current assets: | |
| Cash and cash equivalents (Note 3) | \$ 73,492,198 |
| Short term investments (Note 3) | 1,913,929 |
| Accounts receivable (Note 4) | 5,477,153 |
| Due from the Commonwealth | 1,723,948 |
| Interest receivable | 43,444 |
| Prepaid expenses | 4,671,896 |
| Inventories | 1,702,048 |
| Notes receivable (Note 4) | 1,101,232 |
| Total current assets | <u>90,125,848</u> |
| Noncurrent assets: | |
| Cash and cash equivalents (Note 3) | 21,618,403 |
| Cash with trustees (Note 3) | 6,017,813 |
| Endowment cash and cash equivalents (Note 3) | 354,528 |
| Restricted investments (Note 3) | 1,088,000 |
| Notes receivable (Note 4) | 3,634,636 |
| Capital assets, net (Note 5) | 422,790,468 |
| Total noncurrent assets | <u>455,503,847</u> |
| Total assets | <u>545,629,695</u> |
| LIABILITIES | |
| Current liabilities: | |
| Accounts and retainage payable | 13,444,373 |
| Accrued payroll expense | 17,442,691 |
| Deferred revenue | 11,205,583 |
| Long-term liabilities-current portion | 17,868,122 |
| Due to commonwealth | 165,750 |
| Deposits | 3,010,847 |
| Total current liabilities | <u>63,137,366</u> |
| Noncurrent liabilities (Note 7): | |
| Deferred revenue | 19,817 |
| Long term liabilities | 49,900,293 |
| Due to federal government | 4,501,145 |
| Total noncurrent liabilities | <u>54,421,255</u> |
| Total liabilities | <u>117,558,621</u> |
| NET ASSETS | |
| Invested in capital assets, net of related debt | 385,962,937 |
| Restricted for: | |
| Nonexpendable | 452,391 |
| Expendable | 23,796,947 |
| Unrestricted | 17,858,799 |
| Total net assets | <u>\$ 428,071,074</u> |

The accompanying Notes to the Financial Statements are an integral part of this statement.

VIRGINIA COMMUNITY COLLEGE SYSTEM
STATEMENT OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS
For the Year Ended June 30, 2002

| | |
|--|----------------|
| Operating revenue: | |
| Tuition and fees (net of scholarship allowances of \$26,784,279) | \$ 118,519,493 |
| Federal grants and contracts | 96,195,378 |
| State and local grants | 5,456,131 |
| Nongovernmental grants | 6,563,353 |
| Sales and services of educational departments | 1,984,433 |
| Auxiliary enterprises (net of scholarship allowances of \$3,364,090) | 10,771,152 |
| Other operating revenues | 6,106,957 |
| | <hr/> |
| Total operating revenue | 245,596,897 |
| | <hr/> |
| Operating expenses: | |
| Instruction | 255,085,731 |
| Public service | 4,473,227 |
| Academic support | 53,128,933 |
| Student services | 38,450,235 |
| Institutional support | 90,312,790 |
| Operation and maintenance | 46,293,362 |
| Scholarships and fellowships | 56,670,025 |
| Auxiliary enterprises | 9,660,308 |
| | <hr/> |
| Total operating expenses | 554,074,611 |
| | <hr/> |
| Operating income (loss) | (308,477,714) |
| | <hr/> |
| Nonoperating revenues (expenses): | |
| State appropriations (Note 6) | 307,014,673 |
| Local appropriations | 1,859,179 |
| Grants and gifts | 774,278 |
| Investment income | 1,575,123 |
| Interest on capital asset related debt | (2,182,620) |
| Other nonoperating revenue (expense) | (1,598,432) |
| | <hr/> |
| Total nonoperating revenue | 307,442,201 |
| | <hr/> |
| Income before other revenues | (1,035,513) |
| | <hr/> |
| Capital appropriations | 11,841,973 |
| Capital grants and gifts | 7,512,121 |
| | <hr/> |
| Increase in net assets | 18,318,581 |
| | <hr/> |
| Net assets - beginning of year | 409,752,493 |
| | <hr/> |
| Net assets - end of year | \$ 428,071,074 |
| | <hr/> |

The accompanying Notes to the Financial Statements are an integral part of this statement.

VIRGINIA COMMUNITY COLLEGE SYSTEM
STATEMENT OF CASH FLOWS
For the Year Ended June 30, 2002

| | |
|--|----------------|
| Cash flows from operating activities: | |
| Tuition and fees | \$ 115,275,152 |
| Grants and contracts | 106,771,614 |
| Payments to suppliers and others | (158,848,093) |
| Payments to employees | (378,398,287) |
| Sales and services of educational departments | 1,984,581 |
| Auxiliary enterprises revenues | 10,799,350 |
| Loans issued to students | (1,350,625) |
| Loans collected from students | 1,341,519 |
| Other | 6,586,217 |
| | <hr/> |
| Net cash used by operating activities | (295,838,572) |
| | <hr/> |
| Cash flows from non-capital financing activities: | |
| State appropriations | 307,014,673 |
| Local appropriations | 1,859,179 |
| Grants and gifts | 785,824 |
| Agency expenses | (6,547,540) |
| Agency revenues | 6,645,784 |
| PLUS, Stafford and Direct Lending loan receipts | 2,920,711 |
| PLUS, Stafford and Direct Lending loan disbursements | (2,919,232) |
| Loan receipts | 1,009,665 |
| Loan repayments | (629,225) |
| Other non-operating revenues | 6,729 |
| | <hr/> |
| Net cash flow provided by non-capital financing activities | 310,146,568 |
| | <hr/> |
| Cash flow from capital financing activities: | |
| Capital appropriations | 10,453,429 |
| Capital grants and gifts | 3,926,572 |
| Purchase capital assets | (40,228,161) |
| Proceeds from sale of capital assets | 85,216 |
| Proceeds from bond issue | 7,285,000 |
| Debt interest payments | (1,061,066) |
| Debt principal payments | (7,643,984) |
| | <hr/> |
| Net cash used by capital financing activities | (27,182,994) |
| | <hr/> |
| Cash flow from investing activities: | |
| Purchases of investments | (3,394,739) |
| Sale of investments | 1,730,760 |
| Investment income | 1,586,732 |
| | <hr/> |
| Net cash used by investing activities | (77,247) |
| | <hr/> |
| Net decrease in cash and cash equivalents | (12,952,245) |
| | <hr/> |
| Cash and cash equivalents - beginning of year | 114,435,187 |
| | <hr/> |
| Cash and cash equivalents - end of year | \$ 101,482,942 |
| | <hr/> |

| | |
|---|--------------------------------|
| Reconciliation of operating income (loss) to net cash used in operating activities: | |
| Operating income (loss) | \$ (308,477,714) |
| Adjustment to reconcile operating income (loss) to net cash used in operating activities: | |
| Depreciation expense | 20,689,109 |
| Changes in assets and liabilities: | |
| Accounts receivable, net | (1,645,312) |
| Prepaid expenses and other | (4,679,313) |
| Accrued compensation and other | 1,089,559 |
| Accounts payable | 1,178,280 |
| Deferred revenue | (3,999,142) |
| Deposits pending distribution | <u>5,961</u> |
| Net cash used in operating activities | <u><u>\$ (295,838,572)</u></u> |
| Noncash transactions: | |
| Equipment Trust Fund assets | \$ 3,081,553 |
| Asset acquired through capital leases or installment purchases | \$ 4,389,779 |
| Donated fixed assets | \$ 539,576 |
| Debt principal and interest payments made by Treasury | \$ 1,960,958 |

The accompanying Notes to the Financial Statements are an integral part of this statement.

NOTES TO FINANCIAL STATEMENTS

VIRGINIA COMMUNITY COLLEGE SYSTEM

NOTES TO FINANCIAL STATEMENTS

AS OF JUNE 30, 2002

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

A. Reporting Entity

The Virginia Community College System (VCCS) was established as an institution of higher education in 1965. The System includes the State Board for Community Colleges, a System Office located in Richmond, 23 community colleges located on 40 campuses throughout the Commonwealth, and the Information Technology Utility. The State Board for Community Colleges is the governing body and is charged with the responsibility to establish, control, and administer a statewide system of publicly supported comprehensive community colleges. The System, therefore, functions as a statewide institution of higher learning.

The accompanying financial statements include all of the individual community colleges, the System Office, and the Information Technology Utility under the control of the State Board for Community Colleges. A list of colleges included in this audit is found in the schedule entitled, "Community College Presidents". Each individual college and the System Office have educational foundations that are further described in Note 2. The assets of these educational foundations, which are separately incorporated and managed by their own boards, are not included in these statements.

The VCCS has no component units, as defined by GASB Statement Number 14, *The Financial Reporting Entity*.

The System is a discrete component unit of the Commonwealth of Virginia and is included in the general-purpose financial statements of the Commonwealth. A separate report is prepared for the Commonwealth of Virginia that includes all agencies, boards, commissions, and authorities over which the Commonwealth exercises or has the ability to exercise oversight authority.

B. Accounting Policy Changes

The VCCS adopted the following accounting and reporting change for the year ended June 30, 2002:

GASB Statement Number 34 – *Basic Financial Statements - and Management Discussion and Analysis - for State and Local Governments*, as amended by GASB Statement Number 35 – *Basic Financial Statements - and Management's Discussion and Analysis - for Public Colleges and Universities*. These Statements impose new standards for financial reporting. The fund-group perspective previously required has been replaced with a comprehensive, entity-wide perspective of assets, liabilities, net assets, revenues, expenses, change in net assets, and cash flows. Therefore, the titles and formats of the financial statements have changed significantly. In addition, management is required to provide a

management's discussion and analysis that gives readers an analysis of the overall financial position and results of operations of the VCCS.

The significant changes made in order to comply with the new requirements were recording depreciation on capital assets, reporting tuition and fees net of scholarship discounts and allowances, and recording revenues and expenses related to the summer term that encompasses two fiscal years during the period earned and incurred.

C. Basis of Accounting

For financial reporting purposes, the System is considered a special purpose government engaged in only business-type activities. Business-type activities are those that are financed in whole or in part by fees charged to external parties for goods and services. Accordingly, the financial statements have been presented using the economic resources measurement focus and the accrual basis of accounting. Under the accrual basis, revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. All material internal transactions have been eliminated.

Revenues and expenses of the summer academic term occur within two fiscal years, because the term extends from May through August and the fiscal year ends on June 30. Expenses and an equal amount of revenue have been reported in the current period for the portion of the summer academic term from May 16 through June 30, 2002.

The System has the option to apply all Financial Accounting Standards Board (FASB) pronouncements issued after November 30, 1989, unless FASB conflicts with GASB. The System has elected not to apply FASB pronouncements issued after the applicable date.

D. Inventories

Inventories are stated at cost (primarily first-in, first-out method) and consist mainly of goods purchased for resale and expendable supplies.

E. Investments

Investments meeting the valuation standards outlined in GASB Statement 31, *Accounting and Financial Reporting for Certain Investments and for External Investment Pools*, have been shown at fair market value. The remaining investments have been recorded at cost.

F. Capital Assets

Capital assets consisting of land, buildings, infrastructure, equipment, library books, and construction in progress are stated at appraised historical cost or actual cost where determinable. Improvements to buildings, infrastructure, and land that significantly increase the usefulness, efficiency, or life of the asset are capitalized. Routine maintenance and repairs are charged to operations when incurred. Interest expense relating to construction is capitalized. All equipment purchased under the Equipment Trust Fund program that is titled to the Virginia College Building Authority has been capitalized on these statements. Donated assets are recorded at the estimated fair value at the date of donation. The fixed asset values presented in these financial statements are extracted from the financial data maintained by the

System's Financial Records System and the Fixed Asset Inventory System. Expenditures for equipment are capitalized when the unit acquisition cost is \$5,000 or greater and the estimated useful life is one year or more. Depreciation is calculated using the straight-line method over the estimated useful lives of the assets, generally 50 years for buildings, 20-25 years for infrastructure and land improvements, 3 to 25 years for equipment, and 10 years for library books.

G. Accrued Compensated Absences

The amount of leave earned but not taken by all classified employees, administrative/professional faculty, teaching faculty, and presidents is recorded as a liability on the Statement of Net Assets. The amount reflects, as of June 30, 2002, all unused annual leave, compensatory leave, and the amount payable upon termination under the Commonwealth of Virginia's sick leave pay out policy. An additional liability amount has been included for those employees with less than five years of service based on the probability they will eventually become vested. Also included in the liability is the System's share of employment taxes on leave balances for which employees will be compensated.

H. System Office Expenditures

The Central System Office of the VCCS provides a variety of functions ranging from management control to centralized support services. Because most of these activities are management in nature and cover the operation of the entire System, they have been classified as Institutional Support.

I. Classification of Revenues and Expenses

Operating revenues include activities that have the characteristics of exchange transactions, such as (1) tuition and fees, (2) sales and services of auxiliary enterprises, (3) most federal, state and local grants and (4) contracts and interest on student loans.

Nonoperating revenues include activities that have the characteristics of nonexchange transactions, such as gifts and contributions, as defined by GASB Statement 9, *Reporting Cash Flows of Proprietary Fund Accounting*, and state appropriations and investment income, as defined by GASB Statement 34.

Nonoperating expenses include interest on debt related to the purchase of capital assets and losses on disposal of capital asset. All other expenses are classified as operating expenses.

J. Scholarship Discounts and Allowances

Student tuition and fees revenues, and certain other revenues from students, are reported net of scholarship discounts and allowances in the Statements of Revenue, Expenses, and Changes in Net Assets. Scholarships discounts and allowances are the difference between the stated charge for goods and services provided by the System, and the amount that is paid by students and/or third parties making payments on the student's behalf. Certain governmental grants, such as Pell grants, and other federal, state, or nongovernmental programs are recorded as either operating or nonoperating revenues in the financial statements. To the extent that such revenues are used to satisfy tuition and fees and other student charges, the System has recorded a scholarship discount and allowance.

K. Net Assets

Net assets are classified as follows:

Invested in capital, net of related debt: Consists of capital assets, net of accumulated depreciation and reduced by outstanding debt attributable to the acquisition, construction or improvement of those assets.

Restricted net assets-nonexpendable: Restricted nonexpendable net assets are endowment funds in which donors have stipulated, as a condition of the gifts, that the principal is to remain inviolate in perpetuity and loan funds.

Restricted net assets-expendable: Restricted expendable net assets include resources in which the System is legally or contractually obligated to spend in accordance with restrictions imposed by external third parties.

Unrestricted net assets: Unrestricted net assets represent resources that may be used at the discretion of the governing board for any lawful purpose.

When an expense is incurred that can be paid from either restricted or unrestricted resources, it is the policy of the System to first apply the expense towards restricted resources and then towards unrestricted resources.

As a result of implementing GASB Statement Number 35, beginning fund net assets have been restated as follows:

| | |
|---|-----------------------|
| Combined fund balances, June 30, 2001, as previously reported | \$ 633,649,842 |
| Reclassification of federal loan and other balances | (4,420,709) |
| Deferred revenue | (3,120,283) |
| Adjustment to write-off allowance for doubtful accounts on federal loan balances | 345,226 |
| Adjustment to record accumulated depreciation as of June 30, 2001 | (205,858,350) |
| Adjustment to fixed asset values | (7,141,267) |
| Adjustment to capital lease obligation | (446,143) |
| Adjustment to write-off unbound periodicals | (3,339,065) |
| Adjustment to record previously expensed works of art as non-depreciable capital assets | <u>83,242</u> |
| Combined fund balances, July 1, 2002, restated as net assets | <u>\$ 409,752,493</u> |

2. AFFILIATED ORGANIZATIONS

Each College and the System's Office have organized educational foundations that provide exclusive benefit to the colleges and System. The educational foundations are non-profit organizations created to raise funds supporting college programs, students, and related activities.

Limited members of the College Boards, locally appointed advisory boards of the System, represent the college on the related foundation's governing board. All educational foundations are independently audited. The State Board requires submission of yearly financial statements to the

System's Office. The following is a condensed summary of the financial condition of the foundations at June 30, 2002 except for Danville, John Tyler, New River, and Virginia Western that are as of December 31, 2001.

| | |
|--------------|---------------------|
| Assets | <u>\$76,634,517</u> |
| Liabilities | 1,373,469 |
| Net Assets | <u>75,261,048</u> |
| Total | <u>\$76,634,517</u> |
| Revenues | <u>\$13,556,973</u> |
| Expenditures | <u>\$11,182,900</u> |

3. CASH AND INVESTMENTS

A. Cash and Cash Equivalents

Cash of the Virginia Community College System that is maintained by the Treasurer of Virginia is invested and collateralized pursuant to Section 2.2-1800, et seq., Code of Virginia (1950), as amended, who is responsible for the collection, disbursement, custody and investment of State funds.

Local deposits with banks and savings institutions not with the Treasurer of Virginia are covered by federal depository insurance or collateralized in accordance with the Virginia Security for Public Deposits Act, Section 2.2-4400 et seq. of the Code of Virginia.

Cash equivalents maintained by the System are investments with maturities of less than three months.

B. Investments

Certain deposits and investments are held by the System. Such investments are reported separately from cash and cash equivalents. Investments represent securities with maturities of more than 3 months and for which management intends to hold the securities to maturity.

C. Credit Risk

The System's cash equivalents and investments are categorized below to give an indication of the level of credit risk assumed by the System at June 30, 2002. Credit risk is the risk the System may not be able to obtain possession of its investment instrument or collateral at maturity.

Category 1 - Insured or registered securities or securities held by the Virginia Community College System or its agent in the name of the Virginia Community College System.

Category 2 - Uninsured and unregistered, with securities held by the counterparty's trust department or agent in the name of the Virginia Community College System.

Category 3 - Uninsured and unregistered, with securities held by the counterparty, or by its trust department or agent but not in the name of the Virginia Community College System.

Categorization of cash equivalents and investments held at June 30, 2002:

| | <u>Category 1</u> | <u>Category 2</u> | <u>Category 3</u> | <u>Market Value</u> |
|----------------------------|---------------------|---------------------|---------------------|-----------------------|
| Cash | | | | \$ 65,125,483 |
| Cash equivalents: | | | | |
| Categorized: | | | | |
| U.S. Government Securities | \$ 348,471 | \$ - | \$ - | 348,471 |
| Repurchase Agreements | 2,562,798 | 2,135,642 | 2,435,000 | 7,133,440 |
| Non-Categorized: | | | | |
| Money Market | - | - | - | 618,285 |
| Local Government | | | | |
| Investment Pool | - | - | - | 28,257,263 |
| <u>Investments:</u> | | | | |
| Categorized: | | | | |
| U.S. Government Securities | 2,474,692 | - | - | 2,474,692 |
| Non-Categorized: | | | | |
| Mutual Funds | - | - | - | 527,237 |
| Total | <u>\$ 5,385,961</u> | <u>\$ 2,135,642</u> | <u>\$ 2,435,000</u> | <u>\$ 104,484,871</u> |

4. ALLOWANCE FOR DOUBTFUL ACCOUNTS

The following receivables included an allowance for doubtful accounts at June 30, 2002:

| | |
|---------------------------------------|--------------------|
| Accounts receivable - Gross | \$5,672,174 |
| Less: Allowance for doubtful accounts | <u>(195,021)</u> |
| Accounts receivable - Net | <u>\$5,477,153</u> |
| Notes and loans receivable - Gross | \$4,851,374 |
| Less: Allowance for doubtful accounts | <u>(115,506)</u> |
| Notes receivable - Net | <u>\$4,735,868</u> |

5. CAPITAL ASSETS

Changes in capital assets for the year ended June 30, 2002 are as follows:

| | Beginning Balance | Additions | Transfers from CIP | Retirements | Ending Balance |
|--|----------------------|----------------------|-----------------------|--------------------|-----------------------|
| Capital assets not being depreciated: | | | | | |
| Land | \$ 25,506,822 | \$ 101,615 | \$ - | \$ - | \$ 25,608,437 |
| Inexhaustible works of art | 83,242 | - | - | - | 83,242 |
| Construction in progress | <u>93,145,748</u> | <u>32,160,986</u> | <u>(12,988,395)</u> | - | <u>112,318,339</u> |
| Total capital assets not being depreciated | <u>118,735,812</u> | <u>32,262,601</u> | <u>(12,988,395)</u> | - | <u>138,010,018</u> |
| Other capital assets: | | | | | |
| Buildings | 298,779,554 | 185,949 | 12,495,306 | 64,717 | 311,396,092 |
| Infrastructure | 11,969,467 | 120,486 | 277,966 | 126,351 | 12,241,568 |
| Equipment | 96,703,376 | 14,453,329 | - | 10,412,149 | 100,744,556 |
| Land improvements | 38,724,799 | 825,615 | 215,123 | 19,829 | 39,745,708 |
| Library books | <u>36,386,096</u> | <u>1,938,401</u> | - | <u>1,004,296</u> | <u>37,320,201</u> |
| Total other capital assets | <u>482,563,292</u> | <u>17,523,780</u> | <u>12,988,395</u> | <u>11,627,342</u> | <u>501,448,125</u> |
| Less accumulated depreciation for: | | | | | |
| Buildings | 89,440,921 | 6,788,539 | - | 7,207 | 96,222,253 |
| Infrastructure | 5,288,288 | 582,040 | - | - | 5,870,328 |
| Equipment | 60,644,948 | 11,010,048 | - | 8,855,313 | 62,799,683 |
| Land improvements | 21,576,317 | 817,042 | - | 12,958 | 22,380,401 |
| Library books | <u>28,907,876</u> | <u>1,491,440</u> | - | <u>1,004,306</u> | <u>29,395,010</u> |
| Total accumulated depreciation | <u>205,858,350</u> | <u>20,689,109</u> | - | <u>9,879,784</u> | <u>216,667,675</u> |
| Other capital assets, net | <u>276,704,942</u> | <u>(3,165,329)</u> | <u>12,988,395</u> | <u>1,747,558</u> | <u>284,780,450</u> |
| Total capital assets, net | <u>\$395,440,754</u> | <u>\$ 29,097,272</u> | <u>\$ -</u> | <u>\$1,747,558</u> | <u>\$ 422,790,468</u> |

CIP additions include capitalized interest of \$11,672.

6. STATE APPROPRIATIONS

The System receives state appropriations from the General Fund of the Commonwealth. The Appropriations Act specifies that such unexpended appropriations shall revert, except as specifically provided by the General Assembly, at the end of the biennium. For years ending at the middle of a biennium, unexpended appropriations that have not been approved for reappropriation in the next year by the Governor become part of the General Fund of the Commonwealth and are, therefore, no longer available to the System for disbursement.

During the year ended June 30, 2002, the Virginia Community College System received the following supplemental unrestricted appropriations in accordance with the Appropriation Act of 2001-02, Chapter 1073, Acts of Assembly.

| | |
|--|-----------------------|
| Original Legislative Appropriations | \$ 308,189,922 |
| Less: Revert –delayed opening new space-operating funds | 391,224 |
| Transfer Blue Ridge Community College workforce lease to State Treasury | <u>194,000</u> |
| Appropriated Enrolled Budget Bill | <u>307,604,698</u> |
| Additions: | |
| Transfers from central appropriations: | |
| Classified salary adjustments-annualized | 2,611,395 |
| Employee health care insurance premium increase | 2,243,168 |
| Carryover – unspent appropriations | 9,389,632 |
| Employee deferred compensation savings match | 1,399,060 |
| Less: | |
| General fund reversion | (9,251,570) |
| Prepay FY03 reversions | (5,659,256) |
| VRS rate reduction | (3,339,352) |
| VRS rate suspension-partial | (3,266,422) |
| Retiree health credit savings reversion | (733,267) |
| Higher Education Equipment Trust Fund non-general cash | (512,750) |
| Group Life Rate Suspension-partial year | (218,014) |
| Gas and power savings | (134,589) |
| Integrated human resource information system costs | (128,689) |
| Automobile liability premium savings reversion | (18,856) |
| Indemnity Bond Premium holiday | (10,301) |
| Philpott Manufacturing | (582,000) |
| General fund reversion | <u>(3,438,234)</u> |
| Adjusted Unrestricted Appropriations | <u>\$ 295,954,653</u> |

The VCCS also received restricted appropriations of \$11,060,020 for a total of \$307,014,673.

7. LONG-TERM LIABILITIES

Long-term liability activity for the year ended June 30, 2002 is as follows:

| | Beginning Balance | Additions | Reductions | Ending Balance | Amounts due within one year |
|--|----------------------|---------------------|----------------------|---------------------|-----------------------------------|
| Debt: | | | | | |
| Bonds payable | \$ 2,743,435 | \$ - | \$ 350,247 | \$ 2,393,188 | \$ 366,710 |
| ETF leases | 5,393,603 | - | 3,910,814 | 1,482,789 | 1,482,789 |
| Other capital leases | 25,196,530 | 1,500,886 | 1,118,326 | 25,579,090 | 1,207,914 |
| Installment purchases | 5,715,774 | 2,888,893 | 3,069,105 | 5,535,562 | 1,842,331 |
| Notes payable: | | | | | |
| Pooled bonds | 325,000 | 7,285,000 | 35,000 | 7,575,000 | 35,000 |
| Other notes payable | <u>621,950</u> | <u>1,009,665</u> | <u>629,225</u> | <u>1,002,390</u> | <u>1,002,390</u> |
| Total bonds, notes and capital leases | <u>39,996,292</u> | <u>12,684,444</u> | <u>9,112,717</u> | <u>43,568,019</u> | <u>5,937,134</u> |
| Other liabilities: | | | | | |
| Compensated absences | 23,831,705 | 16,361,311 | 15,992,620 | 24,200,396 | 11,930,988 |
| Liability to federal government | 4,406,506 | 167,376 | 72,737 | 4,501,145 | - |
| Deferred revenue | <u>-</u> | <u>19,817</u> | <u>-</u> | <u>19,817</u> | <u>-</u> |
| Total other liabilities | <u>28,238,211</u> | <u>16,548,504</u> | <u>16,065,357</u> | <u>28,721,358</u> | <u>11,930,988</u> |
| Total long-term liabilities | <u>\$68,234,503</u> | <u>\$29,232,948</u> | <u>\$ 25,178,074</u> | <u>\$72,289,377</u> | <u>\$17,868,122</u> |

8. BONDS PAYABLE

Long-term debt in the form of bonds payable of the System as of June 30, 2002, consists of the following:

Higher Education Bonds, Series 1992A, issued \$3,010,000 to finance construction of a parking deck on the Alexandria campus of Northern Virginia Community College with average coupon interest of 5.40 percent payable semiannually. The final installment of the outstanding balance of \$145,000 is due June 1, 2003.

Higher Education Bonds, Series 1994 (9c), issued \$1,685,000 to finance construction of a parking lot on the Portsmouth campus of Tidewater Community College. The balance is payable in annual installments from \$210,000 to \$225,000 with an average coupon rate of 5.85 percent payable semiannually. The final installment of \$225,000 is due June 1, 2004. The outstanding balance at June 30, 2002 is \$435,000.

Higher Education Refunding Bonds, Series 1999, issued \$1,868,800 to advance refund a portion of the Higher Education Bonds, Series 1992A noted above. The balance is payable in annual installments ranging from approximately \$10,000 to \$240,000 with an average coupon rate of 4.32 percent payable semiannually. The final installment of \$239,167 is due June 1, 2012. The outstanding balance at June 30, 2002 is \$1,813,188.

Aggregate annual maturities of bonds payable for fiscal years after 2002:

| Year Ending June 30 | Principal | Interest | Total |
|------------------------------------|--------------------|------------------|---------------------|
| 2003 | \$ 366,710 | \$115,290 | \$ 482,000 |
| 2004 | 391,660 | 94,258 | 485,918 |
| 2005 | 175,138 | 73,259 | 248,397 |
| 2006 | 178,778 | 65,377 | 244,155 |
| 2007 | 185,934 | 58,047 | 243,981 |
| 2008-2012 | <u>1,094,968</u> | <u>152,308</u> | <u>1,247,276</u> |
| Total debt service Requirements | <u>\$2,393,188</u> | <u>\$558,539</u> | <u>\$ 2,951,727</u> |

9. NOTES PAYABLE

Notes payable represents an agreement with the Virginia Public Building Authority (VPBA) to finance parking improvements for the Midlothian campus of John Tyler Community College. The balance is to be repaid in ten annual installments ranging from \$35,000 to \$45,000 with an average coupon rate of 3.83 percent payable semiannually. The final installment of \$45,000 is due September 1, 2008. The outstanding balance at June 30, 2002 is \$290,000.

Notes payable represents an agreement with the Virginia Public Building Authority (VPBA) to finance the parking garage for the Medical Education campus of Northern Virginia Community College. The balance is to be repaid in twenty annual installments ranging from \$265,000 to \$555,000 with an average coupon rate of 4.61 percent payable annually. The final installment of \$555,000 is due September 1, 2021. The outstanding balance at June 30, 2002 is \$7,285,000.

Other notes payable of \$1,002,390 represents advances received from the Commonwealth of Virginia in anticipation of federal grant funding.

Scheduled maturities of notes payable are as follows:

| Year Ending June 30 | Principal | Interest | Total Payments |
|------------------------|---------------------|---------------------|----------------------|
| 2003 | \$ 1,037,390 | \$ 10,473 | \$ 1,047,863 |
| 2004 | 305,000 | 328,503 | 633,503 |
| 2005 | 310,000 | 319,082 | 629,082 |
| 2006 | 320,000 | 309,472 | 629,472 |
| 2007 | 335,000 | 298,735 | 633,735 |
| 2008-2012 | 1,720,000 | 1,291,905 | 3,011,905 |
| 2013-2017 | 2,020,000 | 896,419 | 2,916,419 |
| 2018-2022 | <u>2,530,000</u> | <u>385,381</u> | <u>2,915,381</u> |
| Totals | <u>\$ 8,577,390</u> | <u>\$ 3,839,970</u> | <u>\$ 12,417,360</u> |

10. LEASE COMMITMENTS AND INSTALLMENT PURCHASES

The System is committed under various capital lease, operating lease, and installment purchase agreements. The cost of assets capitalized under capital lease and installment purchase agreements total \$38,243,418 and \$5,505,349, respectively. Rent expense under operating lease agreements amounted to \$7,011,208 for the year. A summary of future obligations under lease agreements as of June 30, 2002, follows:

| Year Ending June 30 | Operating Lease Obligations | Capital Lease Obligations | Installment Purchase Obligations |
|--|--------------------------------|------------------------------|--|
| 2003 | \$ 1,662,768 | \$ 2,628,718 | \$ 2,024,540 |
| 2004 | 1,447,534 | 2,635,817 | 1,232,432 |
| 2005 | 1,364,047 | 2,639,973 | 1,097,863 |
| 2006 | 836,790 | 2,390,212 | 952,474 |
| 2007 | 675,126 | 2,394,272 | 637,272 |
| 2008-2012 | 5,401,715 | 11,945,584 | 63,232 |
| 2013-2017 | 264,000 | 10,660,526 | - |
| 2018-2022 | <u>-</u> | <u>3,694,685</u> | <u>-</u> |
| Total obligation and gross minimum lease payment | <u>\$ 11,651,980</u> | 38,989,787 | 6,007,813 |
| Less: Interest | | <u>13,410,697</u> | <u>472,251</u> |
| Present value of minimum lease payments | <u>\$ 11,651,980</u> | <u>\$ 25,579,090</u> | <u>\$ 5,535,562</u> |

11. EQUIPMENT TRUST FUND

The System participates in the Higher Education Equipment Trust Fund of the Virginia College Building Authority (VCBA). The Higher Education Equipment Trust Fund provides funds to public colleges and universities for equipment acquisition. In prior years, funds were provided in the form of a lease. During the year ended June 30, 2002, the VCBA financed the ETF program with state funds, which will not require repayment. However, debt obligations are outstanding for prior fiscal years. All remaining obligations under prior lease agreements are due in the fiscal year ending June 30, 2003. The gross minimum lease payments, interest and present value of the minimum lease payments are \$1,553,222, \$70,433 and \$1,482,789, respectively.

12. COMMITMENTS

At June 30, 2002, the VCCS had future commitments for construction contracts totaling approximately \$31,084,642. The System held \$2,888,659 as retainage payable on construction and architectural/engineering contracts for work performed. The retainage payable will be remitted to the various contractors upon satisfactory completion of the construction projects.

13. PENSION PLAN

Employees of the Virginia Community College System are employees of the Commonwealth of Virginia. Substantially all full-time classified salaried employees of the System participate in a defined benefit pension plan administered by the Virginia Retirement System (VRS). VRS is an agent multiple-employer public employee retirement system that acts as a common investment and administrative agency for the Commonwealth of Virginia and its political subdivisions.

The VRS does not measure assets and pension benefit obligations separately for individual State institutions. Information relating to this plan is available at the statewide level only in the Commonwealth of Virginia's Comprehensive Annual Financial Report (CAFR). The Commonwealth, not the VCCS, has overall responsibility for contributions to this plan. The CAFR provides disclosure of the Commonwealth's unfunded pension benefit obligation at June 30, 2002. The same report contains historical trend information showing VRS's progress in accumulating sufficient assets to pay benefits when due.

Most full-time faculty and certain administrative staff participate in one of five optional retirement plans. Each is a fixed-contribution plan where the retirement benefits received are based on the employer's (10.4 percent) contributions, plus interest and dividends. As with VRS, the employees' contributions are assumed by the employer. Individual contracts issued under the ORP plan provide for full and immediate vesting of the VCCS contributions. Total pension costs under this plan were \$3,892,839 and \$3,682,053 for years ended June 30, 2002 and 2001, respectively. Contributions to the ORP plan were calculated using the base salary amount of \$37,431,141 and \$35,404,355 for fiscal years 2002 and 2001. The VCCS total payroll for fiscal years 2002 and 2001 was \$310,355,389 and \$295,370,135 respectively.

14. POST-EMPLOYMENT BENEFITS

The Commonwealth participates in the VRS-administered statewide group life insurance program which provides post-employment life insurance benefits to eligible retired and terminated

employees. The Commonwealth also provides health care credits against the monthly health insurance premiums of its retirees who have at least 15 years of State service and participate in the State's health plan. Information related to these plans is available at the statewide level in the Commonwealth's Comprehensive Annual Financial Report.

15. CONTINGENCIES

Grants

The VCCS receives assistance from non-state grantor agencies in the form of grants. Entitlement to these resources is generally conditional upon compliance with the terms and conditions of grant agreements. Substantially all grants are subject to financial and compliance audits by the grantors. All disallowances as a result of these audits become a liability of the VCCS. As of June 30, 2002, the VCCS estimates that no material liabilities will result from such audits.

Litigation

The VCCS has been named as a defendant in a lawsuit involving a contract dispute with a construction vendor. It is not possible to estimate the loss or range of loss at this time.

16. OPERATING EXPENSES BY NATURAL AND FUNCTIONAL CLASSIFICATIONS

VCCS operating expenses for the year ended June 30, 2002 were as follows:

| Functional Classification | Natural Classification | | | | | Total |
|---------------------------------------|--------------------------|---------------------|----------------------|---------------------|------------------------------------|----------------------|
| | Salaries and benefits | Utilities | Scholarships | Depreciation | Supplies, services and other | |
| Instruction | \$220,883,717 | \$ - | \$ 1,060,950 | \$10,909,386 | \$22,231,678 | \$255,085,731 |
| Public Service | 2,492,167 | - | 230 | 250,173 | 1,730,657 | 4,473,227 |
| Academic Support | 42,098,525 | 22,160 | 131,911 | 3,158,646 | 7,717,691 | 53,128,933 |
| Student Services | 35,379,701 | - | 103,000 | 95,179 | 2,872,355 | 38,450,235 |
| Instructional Support | 65,044,423 | 17,338 | 40,903 | 5,331,112 | 19,879,014 | 90,312,790 |
| Operation and Maintenance of Plant | 12,978,488 | 7,326,544 | 3,999 | 865,987 | 25,118,344 | 46,293,362 |
| Scholarships and Fellowships | - | - | 56,670,025 | - | - | 56,670,025 |
| Auxiliary Enterprises | 1,285,841 | 75,999 | 383,106 | 78,626 | 7,836,736 | 9,660,308 |
| Total Expenses | <u>\$380,162,862</u> | <u>\$ 7,442,041</u> | <u>\$ 58,394,124</u> | <u>\$20,689,109</u> | <u>\$87,386,475</u> | <u>\$554,074,611</u> |

17. RISK MANAGEMENT

The System is exposed to various risks of loss related to torts; theft of, damage to, and destruction of assets; errors and omissions; non-performance of duty; injuries to employees; and natural disasters. The System participates in insurance plans maintained by the Commonwealth of Virginia. The state employee health care and worker's compensation plan are administered by the Department of Human Resource Management and the risk management insurance plans are administered by the Department of Treasury, Division of Risk Management. Risk management insurance includes property, general liability, faithful performance of duty bonds, automobile, and air and watercraft plans. The System pays premiums to each of these Departments for its insurance coverage. Information relating to the Commonwealth's insurance plans is available at the statewide level in the Commonwealth of Virginia's Comprehensive Annual Financial Report.

VIRGINIA COMMUNITY COLLEGE SYSTEM
Richmond, Virginia

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